

Message Text

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C O N F I D E N T I A L STATE 294677

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QUOTE4 C O N F I D E N T I A L STATE 294677

E.O. 11652: GDS TAGS: EMIN EFIN EINV CG US

SUBJECT: FUTURE OF SMTF PROJECT

1) SUMMARY: HIGH-LEVEL SMTF COPPER CONSORTIUM DELEGATION,
LED BY STANDARD OIL OF INDIANA CHAIRMAN SWEARINGEN, IN-
FORMED DEPUTY SECRETARY INGERSOLL DEC 9 THAT CONSORTIUM
TRENDING STRONGLY TOWARD DECISION TO SUSPEND WORK ON
PROJECT UNLESS SOMEONE ELSE IS PREPARED TO PICK UP RISK
ON CONTINUED EXPENDITURE OF \$20 MILLION A MONTH WHILE
ATTEMPT IS MADE TO RESOLVE FINANCING AND OTHER UNCERTAIN-
TIES WHICH NOW ENCUMBER PROJECT. HAVING ALREADY INVESTED
OVER \$200 MILLION -- ABOUT THE TOTAL ORIGINALLY ENVISAGED
-- SHAREHOLDERS NOW FEAR THAT IF THEY GO AHEAD THEY COULD
FIND THEMSELVES FINANCING THE ENTIRE PROJECT, NOW GROWN TO
\$900 MILLION, ON AN EQUITY BASIS OR BEING RESPONSIBLE FOR
THAT AMOUNT UNDER A COMPLETION GUARANTEE EVEN IF PROSPECTIVE
DEBT FINANCING IS OBTAINED. THEY ALSO SEE SIX MONTHS
NEEDED TO CLARIFY MAJOR PROJECT UNCERTAINTIES AND ENVISAGE
POSSIBILITY THAT EVEN THEN, WITH \$120 MILLION MORE SPENT,
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RISKS MIGHT REMAIN UNACCEPTABLE. DEPUTY SECRETARY STRESSED
IMPORTANCE US ATTACHES TO RELATIONS WITH ZAIRE AND POTENT-
IALLY SERIOUS REPERCUSSIONS OF DECISION TO SHUT SMTF PRO-
JECT DOWN. STANDARD OIL DECISION ON PROJECT COULD COME AS

EARLY AS DECEMBER 18 BOARD MEETING. DEPARTMENT BELIEVES FINAL DECISION SHOULD NOT BE MADE BEFORE IBRD HAS HAD

OPPORTUNITY TO COMPLETE ITS REVIEW OF SMTF FINANCING APPLICATION AND CONSORTIUM HAS MET WITH PRINCIPAL INTERESTED FINANCIAL INSTITUTIONS TO VENTILATE ITS PROBLEMS AND EXPLORE POSSIBLE WAYS OF SALVAGING PROJECT. END SUMMARY.

2) REPRESENTATIVES OF SMTF COPPER CONSORTIUM CALLED ON DEPUTY SECRETARY INGERSOLL DEC 9 TO DISCUSS PROJECT'S FUTURE. SMTF GROUP INCLUDED: JOHN SWEARINGEN, CHAIRMAN OF STANDARD OF INDIANA; GAVIN RELLY, EXECUTIVE DIRECTOR OF ANGO-AMERICAN AND A DIRECTOR OF CHARTER CONSOLIDATED; MAURICE TEMPELSMAN; THEODORE SORENSON; AND OTHER STANDARD OF INDIANA AND CHARTER CONSOLIDATED OFFICIALS. ACTING ASSISTANT SECRETARY MULCAHY AND AMBASSADOR CUTLER WERE PRESENT ALSO.

3) SMTF GROUP INFORMED DEPUTY SECRETARY THAT CONSORTIUM DECISION IMMINENT ABOUT WHETHER TO SUSPEND WORK AND PUT PROJECT ON MAINTAINENCE BASIS (ATCOST OF ABOUT \$700,000/MO.), CONTINUE ON AT CURRENT RATE OF INVESTMENT OF \$20 MILLION A MONTH, OR CONTINUE ON AT SOME REDUCED RATE OF CONSTRUCTION AND INVESTMENT. ALTHOUGH DECISION NOT YET MADE, CONSORTIUM REPS MADE IT CLEAR THAT THEIR THINKING IS TRENDING STRONGLY TOWARD A DECISION TO SUSPEND WORK. THIS CHOICE IS BEING CONTEMPLATED WITH FULL RECOGNITION THAT IT MIGHT PROVOKE EXPROPRIATION OF SMTF ASSETS BY GOZ AND THUS BE TANTEMOUNT TO DECISION TO ABANDON \$200 INVESTMENT ALREADY MADE (ABOUT \$80 MILLION EACH BY MAJOR PARTNERS STANDARD AND CHARTER). (COMMENT: WE UNDERSTAND DECISION TO SUSPEND WOULD ALSO CARRY ABOUT \$60 MILLION IN CANCELLATION COSTS. ACCORDING TO TEMPELSMAN, THE MIDDLE COURSE--SLOWING DOWN RATE OF CONSTRUCTION--IS OF QUESTIONABLE FEASIBILITY GIVEN GREAT COMPLEXITY OF INTER-RELATED ENGINEERING/PROCUREMENT/CONSTRUCTION OPERATIONS. CONFIDENTIAL

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ALTHOUGH PLACING PROJECT ON MAINTAINANCE BASIS WOULD PERMIT CONSORTIUM TO RESUME WORK AT SOME FUTURE DATE IF THE ECONOMIC CALCULUS WARRANTED, AND BARRING EXPROPRIATION, STOPPING WORK NOW AND STARTING UP LATER WOULD ADD AN EXTRA \$120 MILLION TO TOTAL PROJECT COST.)

4) CONSIDERATION OF SUSPENSION HAS BEEN FORCED BY COST OVERRUNS, FINANCING UNCERTAINTIES, AND THE UNSETTLED POLITICAL SITUATION IN THE AREA. TOGETHER, THESE HAVE RAISED FOR THE SHAREHOLDERS THE SPECTRE OF HAVING TO FINANCE A \$900 MILLION PROJECT ENTIRELY OUT OF EQUITY OR OF BEING RESPONSIBLE FOR THIS AMOUNT UNDER A COMPLETION GUARANTEE EVEN IF PROSPECTIVE DEBT FINANCING IS OBTAINED.

SMFT REPS OUTLINED FOLLOWING SPECIFIC PROBLEMS:

(A) DISBURSEMENT OF CHASE-SYNDICATED EURODOLLAR LOAN. EVEN IF LOAN AGREEMENT IS SIGNED IN JANUARY, AS NOW TENTATIVELY PLANNED, AND ZAIRE GOES AHEAD WITH IMF AGREEMENT, SMTF DOUBTS BANKS WILL DISBURSE UNTIL ARREARAGES ARE LIQUIDATED OR REFINANCED. SMTF BELIEVES THIS MEANS NO DISBURSEMENT LIKELY FOR SIX MONTHS, THE PERIOD DINI HAS TOLD THEM WOULD BE REQUIRED TO COMPLETE DEBT-RESCHEDULING ELEMENT OF STABILIZATION PROGRAM.

(B) NEED FOR NEW FINANCING. TO TRY BOTH TO SPREAD THE EQUITY, AND THEREFORE THE RISK, AND TO GET NEW LOAN CAPITAL, THE PARTNERS HAVE APPROACHED THE WORLD BANK. PRESIDENT MCNAMARA HAS PROMISED AN EARLY JANUARY DECISION AS TO WHETHER BANK IS INTERESTED AND, IF IT IS, WHETHER IT THINKS IT CAN COME UP WITH THE \$150 TO \$200 MILLION THE PARTNERS ARE LOOKING FOR. (THIS WOULD TAKE FORM OF SOME COMBINATION OF IBRD LENDING AND IFC INVESTMENT, PLUS THIRD-PARTY--MOST LIKELY OPEC--EQUITY AND LENDING FOR WHICH IBRD WOULD ARRANGE.) BOTH RELLY AND TEMPELSMAN DESCRIBED INITIAL CONTACTS WITH IBRD AS ENCOURAGING. HOWEVER, EVEN IF IBRD SHOULD COMMIT ITSELF IN PRINCIPLE, INFUSION OF NEW DEBT AND EQUITY WOULD REQUIRE COMPLETE RESTRUCTURING OF PROJECT FINANCING AND OWNERSHIP AND WOULD REQUIRE MANY MONTHS TO COMPLETE. AND UNTIL DETAILED AGREEMENTS WORKED OUT, NEW MONEY COULD NOT BE COUNTED AS SURE.
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(C) COMPLETION GUARANTEE. EVEN ASSUMING PRESENTLY ARRANGED LOANS ARE SIGNED AND DISBURSED, COMPLETION GUARANTEE IN SECURITY AGREEMENTS OBLIGATES SHAREHOLDERS TO REPAY LOANS THEMSELVES IF THEY DO NOT COMPLETE PROJECT. GIVEN UNCERTAINTIES CREATED BY WAR IN ANGOLA, THEY CAN ENVISAGE POSSIBILITY OF THIS HAPPENING.

(D) FINANCING OF COST OVERRUN ON INGA-SHABA. INGA-SHABA POWER IS ESSENTIAL TO PROJECT, AND SMTF SEES FINANCING OF COST OVERRUN OF OVER \$200 MILLION ON THE POWER LINE AS FAR FROM ASSURED. SMTF REPS EXPRESSED CONCERN ALSO AT PROSPECT OF HAVING TO PAY SHARPLY INCREASED PRICE FOR POWER. THEY CITED EXIM SUGGESTION THAT PRICE MIGHT HAVE TO BE INCREASED FIVE FOLD OVER AMOUNT ORIGINALLY CONTEMPLATED, AS MEANS OF ASSURING FULL PAYOUT TO THE LENDERS TO THE POWER LINE PROJECT. (COMMENT: EXISTING LOAN AGREEMENT RECOGNIZES THAT THERE WILL BE SUBSTANTIAL DEFICITS IN EARLY YEARS AND COMMITS GOZ TO SUPPLEMENT POWER REVENUES TO ASSURE LOAN SERVICING. HOWEVER, GOZ'S ABILITY TO DO THIS IS NOW VERY MUCH IN DOUBT.)

5) SMTF REPS SAID THAT TO CONTINUE PROJECT WHILE AWAIT-

ING CLARIFICATION OF THESE UNCERTAINTIES COULD MEAN PAY-
ING OUT ANOTHER \$120 MILLION OVER THE NEXT SIX MONTHS AND
THEN FINDING THAT SITUATION REMAINED AS BLEAK AS IT IS
TODAY. IN RESPONSE TO A QUESTION, THEY SAID THEY WOULD
STILL BE INCLINED NOT TO PROCEED EVEN IF BY EARLY
JANUARY ZAIRE WERE TO SIGN A LETTER OF COMMITMENT TO THE
IMF, MOST OF THE CHASE-SYNDICATE BANKS WERE TO AGREE TO
WAIVE THE CROSS-DEFAULT CONDITION AND TO DISBURSE, THE
IBRD WERE TO AGREE IN PRINCIPLE TO ARRANGE AN ADDITIONAL
\$200 MILLION IN FINANCING, AND FINANCING OF THE INGA-
SHABA COST OVERRUN WERE AGREED UPON AT A POWER PRICE
WHICH SMTF COULD BEAR. EVEN GIVEN THIS "BEET-POSSIBLE"
TURN OF EVENTS OVER THE NEXT MONTH, MAJOR UNCERTAINTIES
WOULD REMAIN. WITH COST INCREASES REDUCING THE PROFIT-
ABILITY OF THE PROJECT, THERE IS NO LONGER PROSPECTIVE
PAYOFF ATTRACTIVE ENOUGH TO WARRANT THE RISK. SMTF REPS
SAID COPPER PRICE WOULD HAVE TO AVERAGE \$1.15 A POUND
OVER A TEN-YEAR PERIOD TO JUSTIFY THE INVESTMENT. THIS
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IS COMPARABLE, TTEY SAID, TO WHAT WOULD GENERALLY BE RE-
QUIRED FOR NEW INVESTMENTS IN COPPER ELSEWHERE IN THE
WORLD TODAY. BECAUSE OF THE COST OF CARRYING OUT THE
PROJECT UNDER DIFFICULT CIRCUMSTANCES IN ZAIRE, THE
EXCEPTIONALLY RICH TENKE-FUNGURUME DEPOSIT NO LONGER
PROMISES TO BE EXCEPTIONALLY PROFITABLE.

6) DEPUTY SECRETARY TOLD SMTF GROUP THAT USG ATTACHES
CONSIDERABLE IMPORTANCE TO PROJECT, WHICH IS OF GREAT
CONSEQUENCE TO ZAIRE AND THEREFORE A SALIENT ELEMENT IN
US/ZAIRIAN RELATIONS. HE SAID US REGARDS RELATIONSHIP
WITH ZAIRE AS IMPORTANT TO OUR INTERESTS, AND HE SUGGESTED
THAT ECONOMIC CONSEQUENCES OF SHUTDOWN OF SMTF PROJECT
COULD THREATEN PRESENT ZAIRIAN GOVERNMENT. DEPUTY
SECRETARY REVIEWED PROGRESS MADE TOWARD IMF AGREEMENT
AND ON IMPLEMENTATION OF US ECONOMIC ASSISTANCE PACKAGE
FOR ZAIRE. HE SAID, HOWEVER, THAT IF SMTF PROJECT WERE
NO LONGER VIABLE EVEN WITH FINANCING AND IMPROVEMENT OF
ZAIRIAN ECONOMIC SITUATION, THERE WAS NOT MUCH TO TALK
ABOUT.

7) AMB. CUTLER SAID IT WOULD BE VERY DIFFICULT FOR
MOBUTU TO UNDERSTAND MOTHBALLING OF PROJECT AT VERY
MOMENT WHEN HE HAS FINALLY COMMITTED HIMSELF TO ACCEPT-
ING THE IMF FINANCIAL DISCIPLINE WE HAVE BEEN URGING
UPON HIM FOR SO LONG. DEPTOFF POINTED OUT THAT
EXIMBANK, LIKE SMTF, ALREADY HAS OVER \$200 MILLION AT
STAKE, AND EXPRESSED OPINION THAT SMTF WOULD FIND EXIM
READY TO SEEK A REASONABLE COMPROMISE ON POWER COST
ISSUE. HE SAID EXIM WAS CONCERNED WITH NEGOTIATING TERMS

WHICH WOULD PROVIDE SECURITY FOR ITS LOANS, BUT IT COULD

NOT ACCOMPLISH THIS BY INSISTING ON TERMS WHICH WOULD
KILL OFF THE SOURCE OF REVENUE TO SERVICE THE LOANS.

8) SMTF GROUP EXPRESSED CONCERN ABOUT HOW THEY WOULD
INFORM MOBUTU IF DECISION WERE TAKEN TO SUSPEND PROJECT
WORK. TEMPELSMAN REPORTED HIS DISCUSSIONS WITH MOBUTU
ABOUT POSTPONEMENT OF LOAN SIGNINGS BUT ACKNOWLEDGED
THAT DECISION TO MOTHBALL PROJECT WOULD COME AS COMPLETE
SURPRISE TO HIM. SWEARINGEN PROMISED TO ADVISE DEPT.
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AS SOON AS DECISION MADE AND ASKED THAT USG NOT ALERT
GOZ TO POSSIBILITY OF CLOSEDOWN BEFORE THEN.

9) CONCLUDING, RELLY COMMENTED THAT CONSORTIUM WOULD OF
COURSE BE WILLING TO CARRY ON WORK DURING THE MONTHS
WHICH WOULD BE REQUIRED TO RESTRUCTURE THE FINANCING AND
RESOLVE THE OTHER UNCERTAINTIES IF SOMEONE ELSE WERE
WILLING TO TAKE THE RISK ON THE \$20 MILLION A MONTH IN
NEW EXPENDITURES. TEMPELSMAN HAS SINCE INFORMED THE
DEPT. THAT CONSORTIUM PLANS ASK MCNAMARA, EVEN
BEFORE HIS STAFF HAS COMPLETED ITS REVIEW OF THE PROJECT,
WHETHER IBRD WOULD BE WILLING TO DO THIS.

10) COMMENT: (A) SWEARINGEN, RELLY AND COMPANY GAVE
IMPRESSION OF BEING PSYCHOLOGICALLY PREPARED TO WRITE
OFF \$200 MILLION INVESTMENT. THE PICTURE WHICH THEY
PRESENTED WAS CLEARLY A WORST-CASE ANALYSIS. (IT IS OUR
IMPRESSION, FOR EXAMPLE, THAT SEVERAL OF THE BANKS, AS
WELL AS EXPORT CREDIT AGENCIES, WOULD BE PREPARED TO
DISBURSE IN JANUARY IF ZAIRE SIGNS WITH THE IMF AS
EXPECTED.) ALTHOUGH A FEW WEEKS AGO CHARTER SEEMED TO
BE LESS BEARISH ABOUT THE PROJECT THAN STANDARD, NO
DIFFERENCE IN THE COMPANIES' POSITIONS WAS APPARENT IN
THE MEETING WITH THE DEPUTY SECRETARY. WE UNDERSTAND
FROM TEMPELSMAN THAT STANDARD MAY MAKE ITS DECISION AT
BOARD MEETING DEC. 18 OR PERHAPS SOMEWHAT LATER
DEPENDING UPON TIMING OF APPROACH TO MCNAMARA DESCRIBED
PARA 9 ABOVE.

(B) APPROACH TO MCNAMARA TO ASK FOR GUARANTEE OF
INTERMIM FINANCING EVEN BEFORE IBRD HAS COMPLETED ITS
REVIEW OF PROJECT SEEMS PREMATURE. A MORE SENSIBLE
COURSE, WE WOULD THINK WOULD BE TO AWAIT COMPLETION OF
IBRD REVIEW IN EARLY JANUARY AND THEN, IF IBRD IS WILL-
ING IN PRINCIPLE TO COMMIT ITSELF TO PROJECT, TO BRING
TOGETHER PRINCIPAL INTERESTED PARTIES--PERHAPS IBRD,
EXIM, CHASE, OPIC AND ALSO IMF, GIVEN CRITICAL IMPORT-

ANCE OF SMTF TO ZAIRE'S FINANCIAL FUTURE--TO EXPLORE
WITH SMTF FULL RANGE OF PROBLEMS THEY FACE AND POSSIBLE

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WAYS OF SALVAGING PROJECT. BY EARLY JANUARY, ALSO,
ALL PREPARATORY WORK FOR STABILIZATION PROGRAM SHOULD
HAVE BEEN COMPLETED AND QUESTION OF WHETHER OR NOT
BANKS IN CHASE CONSORTIUM WILL WAIVE CROSS-DEFAULT
CLAUSE AND DISBURSE SHOULD BE CLEARER. DEPT. IS
CONSIDERING HOW SUCH A SCENARIO MIGHT BE BROUGHT ABOUT.
SISCO UNQUOTE KISSINGER

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